IN THE

# Supreme Court of the United States

OCTOBER TERM, 1941.

No. [redacted] 120

BEN BIMBERG & CO., INC.,
*Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,
*Respondent.*

***Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.***

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BEN BIMBERG & CO., INC.,
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*Respondent.*

No. .....

## Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

The petitioner, Ben Bimberg & Co., Inc. prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above case on March 7, 1942, 126 F. (2d) 412, affirming the memorandum decision of the United States Board of Tax Appeals of April 21, 1941. Petition for rehearing was filed March 20, 1942 and on March 27, 1942 the petition was denied. A second petition for rehearing was filed on May 14, 1942 and on May 23, 1942 the petition was denied.

### Summary Statement of the Matter Involved.

Petitioner is a wholesaler and jobber of cotton goods. Its general practice is to obtain orders from its customers

for specific merchandise and then place the orders with well-known mills. When these mills are ready to ship the goods, they ship them directly to the customers for the account of petitioner. The mill or other supplier sends an invoice to petitioner, and petitioner simultaneously invoices its customer with the goods in question. In some instances petitioner fills orders from a small inventory kept on hand (R. 22).

In the latter part of 1935, members of the cotton industry believed that the Agricultural Adjustment Act would be invalidated by the Supreme Court. Petitioner and other firms in the cotton market accordingly had their vendors include in their purchase contracts so-called "Charlotte clauses" which provided that if the Act were invalidated, the amount of processing taxes included in the purchase price of the cotton involved would be refunded to petitioner, or credited on the price if the goods had not yet been paid for (R. 22).

After the Supreme Court invalidated the Agricultural Adjustment Act on January 6, 1936, such vendors as had agreed to include the above-mentioned clause in petitioner's purchase contracts promptly issued purchase allowances or credits to petitioner. Petitioner maintained open accounts with its vendors, and while it received some actual cash refunds, most of the refunds were in the form of credit memoranda, which were used to reduce accounts payable owing by petitioner to its vendors (R. 23).

Pursuant to the aforesaid tax clauses, petitioner received during 1936 from its vendors reimbursements or credits in the total sum of $19,763.13 which was the amount of processing taxes charged to petitioner, although unpaid by the mills, on goods shipped to petitioner's accounts during the 90-day period prior to January 6, 1936. These reimbursements and allowances were applicable to cotton goods purchased by petitioner prior to

December 31, 1935 and, with certain small exceptions, sold by it before that date (R. 23).

Of the sum of $19,763.13 which petitioner received as reimbursements or credits from its vendors, the amount of $7,729.45 was originally reported as income for 1936 and a tax was paid on it. The balance of $12,033.68 was not reported as income for that year. Petitioner had executed credit memos in that latter amount all dated in 1936, drawn to its vendees for the equivalent of the processing taxes included in the purchase price of purchases made by them for 90 days prior to January 6, 1936. On March 15, 1937, petitioner cancelled all of the credit memos in the total amount of $12,033.68 (R. 23).

The petitioner's books, which were kept on the accrual basis, did show the full amount of taxes in question, $19,763.13 as a deduction from gross income. In determining its taxable income for the year 1935, petitioner had included the sum of $19,763.13 (for which sum petitioner was subsequently reimbursed by its vendors as aforesaid) as part of the cost of goods sold (R. 24).

Petitioner has at all times kept its books on an accrual basis (R. 24).

The United States Board of Tax Appeals sustained the action of the Commissioner in imposing a 25% delinquency penalty for late filing of the 1936 tax return stating that there was not "reasonable cause" within Section 291 of the Revenue Act of 1936 (R. 25).

## Jurisdiction.

The jurisdiction of this Court is invoked under the Act of February 13, 1925 (C. 229, 43 Stat. 938) amending the Judicial Code, Section 240; Title 28 U. S. C. A. Section 347. The judgment sought to be reviewed is that of the United States Circuit Court of Appeals for the Second Circuit entered on March 7, 1942, 126 F. (2d) 412,

affirming the memorandum decision of the United States Board of Tax Appeals of April 21, 1941.

## Questions Presented.

1. Were the reimbursements received by petitioner from its vendors income in the year 1935 or 1937, and not in the year 1936?
2. If the reimbursements were income in 1935, is it sufficient if petitioner give the Commissioner an adequate opportunity to readjust the 1935 tax return?
3. Is petitioner entitled to a refund of income tax paid for the year 1936 in the amount of $954.60?
4. Is the petitioner correct in disputing the imposition of a deficiency in income tax for the calendar year 1936, at least as to reimbursements received in the amount of $12,033.68?
5. Is the petitioner correct in asserting that no penalty is due for the calendar year 1936?

## Reasons Relied Upon for the Allowance of the Writ.

### I.

The Court below has ruled on an important question of federal law which has not been, but should be, settled by this court. The question is: Whether a taxpayer who has subsequently been given a refund or reimbursement due to the unconstitutionality of a statute must bring the refund or reimbursement to the Commissioner's notice as soon as he receives it, if he wishes to have his earlier tax return readjusted, or on the other hand, must merely give the Commissioner an adequate opportunity to read-

just the earlier return at any reasonable time before the statute of limitations has run. The Court below adopted the former view which the petitioner considers to be erroneous, harsh and arbitrary.

It is the petitioner's contention that the Commissioner should cancel a deduction taken in one year for an expense which the taxpayer has accrued or paid where the expense item has been refunded in a later year (because it was unlawfully superimposed on a purchase contract or group of contracts) if the statute of limitations has not yet run. It is also the petitioner's position that so long as the taxpayer gives the Commissioner an adequate opportunity to readjust the earlier year before the statute of limitations has run, that suffices on the issue of notice to the Commissioner. In the instant case the petitioner did in fact give the Commissioner several adequate opportunities to readjust its prior income tax return for 1935 long before the statute of limitations had run to prevent such reassessment (R. 40, 42-43).

Because of the numerous cases that concern refunds under the Agricultural Adjustment Act and other unconstitutional statutes where at the time that the refund or reimbursement is made the statute of limitations is yet no bar to a readjustment of the earlier return it is respectfully submitted that the Supreme Court should decide this question: Whether a taxpayer to obtain a reassessment must notify the Commissioner of his refund as soon as it is received, or on the other hand, must merely give the Commissioner an adequate opportunity through notice, before the statute of limitations has run, to readjust the earlier return. Petitioner submits the latter is the correct and more equitable view; and furthermore, that in the instant case such adequate notice and opportunity was afforded to the Commissioner.

## II.

The decision of the Court below if construed to mean that the Commissioner, even though the earlier year is still open, may at his pleasure reassess the original tax or include the refund in the income for the later year is not only in conflict with the decisions of the First and Fourth Circuit Courts of Appeal in *Leach* v. *Commissioner*, 50 F. (2d) 371 (1931 C. C. H. Par. 9416) and *Inland Products Co.* v. *Blair*, 31 F. (2d) 867 (1 U. S. T. C. Par. 390) respectively, but establishes an arbitrary, capricious and one-sided doctrine not sustained by any of the cases.

If the Court below disagreed with the aforesaid cases, it did so on the basis of no cited authority. The cases of *Houbigant, Inc.* v. *Commissioner*, 31 B. T. A. 954, aff. *per curiam*, 80 F. (2d) 1012, cert. denied, 298 U. S. 669, *Nash* v. *Commissioner*, 88 F. (2d) 477 (C. C. A. 7) (37-1 U. S. T. C. Par. 9091), cert. denied 301 U S. 700, *Union Trust Co.* v. *Commissioner*, 111 F. (2d) 60 (C. C. A. 7) (40-1 U. S. T. C. Par. 9273) were recognized by the Court below as distinguishable from the instant case and the *Leach* and *Inland Products Co.* cases, for in those cases the time had passed to assess a deficiency for the earlier year and thus the Courts allowed the Commissioner to surcharge the income for the year of the refund. However, in the present case, as in the *Leach* and *Inland Products Co.* cases, the earlier year was still open and the statute of limitations did not prevent a reassessment of the earlier return.

## III.

It is well settled law among the lower courts that the Commissioner should readjust the original deduction on account of refunds of taxes illegally assessed and col-

lected, where correction of the prior return is not prevented by the statute of limitations.

See:

*Inland Products Co.* v. *Blair,* 31 F. (2d) 867 (C. C. A. 4, 1929);
*Bergan* v. *Commissioner,* 80 F. (2d) 89 (C. C. A. 2, 1935);
*Leach* v. *Commissioner,* 50 F. (2d) 371 (C. C. A. 1, 1931);
*Bohemian Breweries, Inc.* v. *United States,* 27 F. Supp. 588, 89 Ct. Cl. 57 (1939);
*E. B. Elliott Co.* v. *Commissioner,* 45 B. T. A. 82 (1941).

It is also established law among the lower courts that where an additional assessment has been barred by the expiration of the period of limitation the refund is considered as income for the year in which the refund took place (except if the year in which the tax was first paid resulted in a net deficit).

See:

*Houbigant, Inc.* v. *Commissioner, supra;*
*Nash* v. *Commissioner, supra;*
*Union Trust Co.* v. *Commissioner, supra.*

Petitioner must point out that the *Houbigant* and *Nash* cases, wherein the Supreme Court denied certiorari, were both cases where the statute of limitations prevented a reassessment of the earlier return unlike the situation in the instant case, and secondly, an issue in those cases, not involved in the present case, was whether there was a return of capital or income.

In the instant case the earlier year 1935 was still open and the statute of limitations did not prevent a reassess-

ment of the earlier tax year. Too, the petitioner does not dispute the fact that the reimbursements are income; the question here is for what year are they to be treated as income.

The history of the Treasury Department's rulings since 1920 reveals the aforesaid principles to be the policy advocated by the Treasury itself.

O. D. 741, C. B. 3, p. 115 (July-December, 1920);
Mim. 3958, C. B. XI-2, p. 33 (July-December, 1932);
Mim. 4564, C. B. 1937-1, p. 93.

The cases involving A. A. A. reimbursements should adhere to the same doctrine discussed above; namely, that a refund of an unconstitutional or erroneously paid tax is income in the year the refund is received when the year of deduction is barred by the statute of limitations; but that when the year of deduction is not outlawed the income for such year should be adjusted to include the amount of refunded taxes.

Furthermore, the United States Board of Tax Appeals has consistently held that it is proper for a first processor to accrue the amounts to be paid out to its vendees under "Charlotte clauses" as an expense or set-off against sales for the year 1935.

See:

*Sanford Cotton Mills, Inc.* v. *Commissioner,* 42 B. T. A. 190 (1940), (N. A.) 1940-2 C. B. 14, and G. C. M. 22404, 1940-2 C. B. 204, I. T. 3430, 1940-2 C. B. 205 (No Appeal):
*Cartex Mills, Inc.* v. *Commissioner,* 42 B. T. A. 894 (1940), (N. A.) 1940-2 C. B. 9;
*Smith Packing Co.* v. *Commissioner,* 42 B. T. A. 1054 (1940);

*Cannon Valley Milling Co.* v. *Commissioner,* 44 B. T. A. 763 (1941), (N. A.) 1941 P-H par. 66, 367, App. (C) July 14, 1941 (C. C. A. 8);
*Security Flour Mills Co.* v. *Commissioner,* 45 B. T. A. 671 (1941), (N. A.) 1942 P-H par. 66,094, App. (T) Feb. 11, 1942 (C. C. A. 10), App. (C) Mar. 26, 1942 (C. C. A. 10).

If it is proper as a matter of practical accounting for a vendor to accrue the amounts to be paid out to its vendees under "Charlotte clauses" as an expense or setoff against sales for the year 1935, it would follow as a necessary corollary that petitioner, as vendee, should accrue these reimbursements as income or a reduction of costs in the same year. Where both the first processor and its vendee are on the accrual basis, it would unnecessarily complicate accounting practice to hold the obligation of the vendor to make a refund was accruable in 1935, but that the right of receipt of the vendee could not be accrued in the year 1935. All of the events in the instant case relate to 1935, at least as much as in the cases of *Sanford Cotton Mills, Inc., Cartex Mills, Inc., Smith Packing Co.* and *Cannon Valley Milling Co., supra.*

An illustration of such proper accounting practice can be found, among other fields, in the field of mortgages. When the mortgagor on the accrual basis is entitled to a deduction for interest accrued in one year, the mortgagee also on the accrual basis is deemed to have received income in that very same year.

*Cf*: *Midland Mutual Life Insurance Co.* v. *Commissioner,* 300 U. S. 216, 57 Sup. Ct. 423, reh. denied 300 U. S. 688, 57 Sup. Ct. 752.

In *Sanford Cotton Mills, Inc., supra,* the Board of Tax Appeals held that a first processor who made reimburse-

ments to its vendees in 1936 under the so-called "Charlotte clauses" (whose vendees were in the same position as petitioner), could properly accrue this expense for the year 1935 rather than in 1936. The Board so held because, as a practical matter, all the essential facts related to 1935 and the only event which occurred in 1936 was the decision of the Supreme Court invalidating the Agricultural Adjustment Act. Although this case was nonacquiesced, the Government did not take an appeal and the Bureau in effect adopted the decision in G. C. M. 22404, 1940-2 C. B. 204 and I. T. 3430, 1940-2 C. B. 205.

The Board of Tax Appeals in its opinion attempted to distinguish the instant case from *Sanford Cotton Mills, Inc.* and *Cartex Mills, Inc., supra,* on the ground that in those cases the first processors

> "had accrued liabilities to pay sums in either of two events: if the processing tax were upheld, they were obligated to pay the tax to the Government; if it were held invalid, they were under a similar obligation to refund the amount of the tax to their vendees. In other words, the obligation to pay the amount of the taxes to somebody was fixed, in any event, in 1935" (R. 24).

However, the facts in the *Sanford Cotton Mills, Inc.* case, *supra,* do not warrant this distinction. In that case, the Board stated, p. 191;

> "In closing its 1935 accounts, which it did early in 1936, petitioner canceled the aforesaid accrual of $64,599.25 (which it had not paid) as its liability to the United States for tax on cotton processed in 1935, and substituted $22,468.12 which was the amount of its contractual liability for readjustment

to its vendees. This contractual liability it actually discharged in the first seven months of 1936."

It is thus apparent that the amount of accrual was not fixed and payable at all events, but that a liability accrued on the books of the corporation was subsequently canceled and an entirely different liability in a much less amount was substituted therefor. There was a difference of $42,131.13 between the two liabilities, which sum was subsequently reflected on the books of the corporation as an increase of net income for 1935.

The foregoing summary review of the cases and precedents show that the taxpayer is fully justified in its claim that the A. A. A. reimbursements of $19,763.13 are not taxable as income in 1936.

***Wherefore, it is respectfully submitted that the petition should be granted.***

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IN THE

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No. [redacted] 120

BEN BIMBERG & CO., INC.,
*Petitioner,*

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*Respondent.*

## *Brief in Support of Petition for Writ of Certiorari.*

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## Brief in Support of Petition for Writ of Certiorari.

### Opinion Below.

The judgment sought to be reviewed is that of the United States Circuit Court of Appeals for the Second Circuit, entered on March 7, 1942, reported at 126 F. (2d) 412, affirming the memorandum decision of the United States Board of Tax Appeals of April 21, 1941.

### Jurisdiction.

The jurisdiction of this court is invoked under the Act of February 13, 1925 (C. 229, 43 Stat. 938) amending the Judicial Code, Section 240; Title 28 U. S. C. A. Section 347.

## Statement of the Case.

To avoid undue repetition, counsel merely refers the Honorable Court to the Summary Statement of the Matter Involved in the petition for writ of certiorari.

## Specification of Errors.

### I.

The court below erred in holding that before the statute of limitations has run preventing a reassessment of the earlier return (1935) the Commissioner may at his pleasure either reassess the original tax or include the refund in the income for the later year (1936).

### II.

The court below erred in holding that the taxpayer in order to obtain a reassessment of the earlier return when the statute of limitations is no bar must bring the refund to the Commissioner's notice as soon as it is received.

### III.

The court below erred in failing to hold that the taxpayer gave the Commissioner an adequate opportunity before the statute of limitations had run to readjust the earlier return.

### IV.

The court below erred in failing to hold that a taxpayer who gives the Commissioner an adequate opportunity before the statute of limitations has run to readjust the earlier return may compel the Commissioner to reassess the original tax.

**V.**

The court below erred in affirming the decision of the United States Board of Tax Appeals which decision also imposed a 25% delinquency penalty on the taxpayer.

## Summary of Argument.

It is the petitioner's position that the Commissioner should have readjusted the original deduction in the 1935 tax return on account of the refund of taxes illegally imposed since the correction of that return was not prevented by the statute of limitations.

The petitioner gave the Commissioner an adequate opportunity to readjust the 1935 return before the statute of limitations had run and such should suffice on the issue of notice to the Commissioner.

The Commissioner, before the statute of limitations has run, should not at his pleasure be permitted to either reassess the original tax or include the refund in the income for the later year.

## *ARGUMENT.*

### POINT I.

**The Commissioner should have readjusted the original deduction in the 1935 tax return since the correction of that return was not prevented by the statute of limitations.**

The rule of law as laid down by the courts is that where a tax which was deducted from income is refunded in a subsequent year due to the unconstitutionality of the statute under which the tax is imposed, the Commissioner

should readjust the earlier return and include the refund therein when correction of that return is not prevented by the statute of limitations.

*Inland Products Co.* v. *Blair,* 31 F. (2d) 867 (C. C. A. 4, 1929) (1 U. S. T. C. Par. 390);
*Bergan* v. *Commissioner,* 80 F. (2d) 89 (C. C. A. 2, 1935);
*Leach* v. *Commissioner,* 50 F. (2d) 371 (C. C. A. 1, 1931) (C. C. H. Par. 9416);
*Bohemian Breweries, Inc.* v. *United States,* 27 F. Supp. 588, 89 Ct. Cl. 57 (1939);
*E. B. Elliott Co.* v. *Commissioner,* 45 B. T. A. 82 (1941).

In *Inland Products Co.* v. *Blair, supra,* Judge Parker pointed out that the whole question involved was one of correction of mistake and to readjust the returns for the earlier years by eliminating the deduction in question would place both parties to the mistake exactly where they would have been if it had not occurred.

Accord: Mim. 3958, C. B. XI-2, p. 33 (July-December, 1932).

The rationale of the aforesaid rule of law is that the deduction claimed turns out to have been improper and illegal, and since the mistake has been discovered within the time alloted for correction, the return in which the deduction was claimed should be readjusted.

In *J. A. Dougherty's Sons, Inc.* v. *Commissioner,* 121 F. (2d) 700 (1941) (41-2 U. S. T. C. Par. 9562) the issue was whether deductions were properly taken in the prior years. The court permitted a deduction from gross income of accruals made for taxes imposed by a state statute subsequently declared unconstitutional. The provo-

cation for reaching such a result was very great and the Third Circuit, speaking through Judge Jones, stated, p. 10, 346:

> "The particular hardship to the taxpayer * * * grows out of the fact that the Pennsylvania Tax Act was declared unconstitutional in a year subsequent to the taxable years in which the accruals were made, while in the meantime the federal tax on undistributed profits had been enacted and had become effective in the year 1936. Hence, the taxpayer's necessary accrual on its books of the Pennsylvania floor taxes for the respective years rendered the sums so accrued unavailable for dividend distribution in the taxable years. The effect, therefore, of the Commissioner's ultimate disallowance of the taxpayer's deductions for the accrued 1936 and 1937 floor taxes is to restore earnings, *pro tanto*, to those years and at once render them subject to the federal undistributed profits tax * * *. There is evidence in the case * * * that, except for the Pennsylvania floor tax, dividends would have been declared and paid by the taxpayer in 1936 and 1937 to an extent at least equal to the amount of the floor taxes accrued for those years. The taxpayer argues that, in such event, it would never have been subject to surtaxes on undistributed profits for 1936 and 1937, had it been free to distribute its earnings without thought for accruals on account of the Pennsylvania floor taxes."

Furthermore, the *Dougherty* case did not proceed on the basis of correction of a mistake but according to Judge Learned Hand seemed to rely on some language in *Chicot County Drainage* v. *Baxter State Bank*, 308 U.

S. 371, to the effect that an unconstitutional tax is not quite a nullity, but lives in Limbo, as it were, until the court puts an end to it (R. 35).

*Contra*:

*Norton* v. *Shelby County,* 118 U. S. 425, 442;
*Chicago, Indianapolis & Louisville R. R. Co.* v. *Hackett,* 228 U. S. 559, 566;
*Louisville Gas & Electric Co.* v. *Coleman,* 277 U. S. 32;
*Frost* v. *Corporation Commission of Oklahoma,* 278 U. S. 515.

Judge Learned Hand, speaking for the court below, said: "* * * we are disposed to consider the decision as not generally contradicting the power of the Commissioner to cancel such a deduction" (R. 35).

The case of *Commissioner* v. *Central United National Bank,* 99 F. (2d) 568 (C. C. A. 6) (38—2 U. S. T. C. Par. 9562) was recognized by Judge Hicks therein as different from the *Inland Products Co.,* the *Leach* and *Bergan* cases, *supra,* on which cases petitioner here relies, for unlike those cases, the *Central United National Bank* case involved a tax deducted which finally turned out to be lawful. Judge Hicks stated, p. 10, 677:

> "In the *Blair* case there was an erroneous assessment and payment of taxes, and the court held that the taxpayer could not take deductions therefor after the illegal taxes had been refunded.
>
> "The question in the *Leach* and *Bergan* cases was similar to that in the *Blair* case. It has but little analogy to the issue here."

The Treasury Department's rulings since 1920 support the contention of the petitioner that the Commis-

sioner should readjust the original deduction on account of refunds of taxes illegally assessed and collected, where correction of the prior return is not prevented by the statute of limitations.

In O. D. 741, C. B. 3, p. 115 (July-December, 1920) the ruling held that excess customs duties, which were paid during the years 1915, 1916, and 1917 and for which a refund was received during the year 1919, were amounts which had been erroneously deducted in computing net income for the years 1915, 1916, and 1917, respectively, rather than an amount representing income for the year 1919.

In Mim. 3958, C. B. XI-2, p. 33 (July-December, 1932) the Treasury Department approved of the *Inland Products Co.* case, *supra,* and further stated that legal and proper collections of customs duties and taxes should be distinguished from those illegally or improperly made. In the case of the former, any refund thereof does not constitute the correction of a mistake because no mistake has been made (viz: the drawback provisions of the law where the importer pays the customs duties, but later secures a refund by showing that the goods imported on which the duties were paid have gone into a manufactured article which was later exported). The Treasury concluded that refunds of customs duties or taxes, the collection of which was legally or properly made, should be treated as income for the year in which refunded.

The Treasury in Mim. 4564, C. B. 1937-1, p. 93, stated:

> " * * * in the case of a refund in any year of customs duties or taxes illegally assessed and collected which have been taken as deductions in Federal income tax returns for a prior year, if the taxable year in which the deduction was taken is closed

by the expiration of the period of limitations for the making of an additional assessment of income tax * * *, the refund shall be treated as income for the taxable year in which it was made.

"Refunds of customs duties and taxes legally collected which have been taken as deductions in Federal income tax returns for a prior year should continue to be treated in all cases as income for the taxable year in which the refund is made * * *."

(See: 1942 P-H pp. 7173-4, par. 7301.)

The situation in the processing tax reimbursement cases is like that where a tax has been illegally collected or paid under mistake in one year, and refunded in a subsequent year. The processing tax reimbursement cases should logically adhere to the same doctrine and in the instance where the statute of limitations is no bar the subsequent refund or reimbursements should be adjusted as of the year when the tax was paid or deduction taken, in order to properly reflect the income for that year.

The Board of Tax Appeals relied mainly on the decisions of *North American Oil Consolidated* v. *Burnet*, 282 U. S. 417, and *Burnet* v. *Sanford & Brooks*, 282 U. S. 359, as supporting its determination that the reimbursements received should have been accrued as income for 1936. However, the general rules set forth in those cases have no application to the circumstances involved in the instant case. Those decisions did not involve a refund in a subsequent year of an illegally collected tax when a correction of the earlier return was still possible and the Circuit Court of Appeals below apparently recognized this distinction. Furthermore, the Board itself has in a number of recent cases similar to the present case recognized that the rules set forth in the *Burnet* and *North American* cases, *supra*, do not apply.

See:

*Sanford Cotton Mills, Inc.* v. *Commissioner,* 42 B. T. A. 190 (1940), (N. A.) 1940-2 C. B. 14 and G. C. M. 22404, 1940-2 C. B. 204, I. T. 3430, 1940-2 C. B. 205 (No Appeal);

*Cartex Mills, Inc.* v. *Commissioner,* 42 B. T. A. 894 (1940), (N. A.) 1940-2 C. B. 9;

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*Security Flour Mills Co.* v. *Commissioner,* 45 B. T. A. 671 (1941), (N. A.) 1942 P-H par. 66,094, App. (T) Feb. 11, 1942 (C. C. A. 10), App. (C) Mar. 26, 1942 (C. C. A. 10).

In *Smith Packing Co., supra,* taxpayer, shortly after the processing tax under the Agricultural Adjustment Act was invalidated on January 6, 1936, received from a bank an amount of money which had been held in escrow for taxpayer's account in 1935, pending the outcome of litigation concerning the validity of the processing tax. The Board held that the Commissioner was in error in including the amount in question as taxable income for 1936.

In *Cannon Valley Milling Co., supra,* taxpayer, a first processor, during its fiscal year ended in 1937, reimbursed its vendees for processing taxes included in the price of wheat products sold to them in May and June 1935. The Board held that in order to clearly reflect the taxpayer's income for the fiscal year ended June 30, 1935, such reimbursements were deductible in computing its net income for that year since they represented payments relating to the claims on 1935 sales and were not related to sales made in 1937.

The petitioner's position is as follows: If it is proper as a matter of practical accounting for a vendor to accrue the amounts to be paid to the vendees under "Charlotte clauses" as an expense or setoff against sales for the year 1935, it would follow as a necessary corollary that petitioner, as vendee, should accrue these reimbursements as income or a reduction of costs in the same year Where both the first processor and its vendee are on the accrual basis, it would be illogical as well as improper accounting practice to hold that the obligation of the vendor to make payment was accruable in 1935 but that the right of receipt of the vendee could not be accrued in the year 1935.

See also:

*Ada Milling Co.* v. *Commissioner,* 45 B. T. A. Memorandum Opinion, Docket No. 100,466, 1941 P-H par. 65,018, reported in full 1941 P-H B. T. A. Memo. Service, par. 41,502;

*Athens Roller Mills, Inc.* v. *Commissioner,* 46 B. T. A. No. 135, 1942 C. C. H. par. 7,507 (April 28, 1942);

*Flour Finance Co.* v. *Commissioner,* 46 B. T. A. Memorandum Opinion, Docket No. 105,206, 1942 C. C. H. par. 7,502-C (April 17, 1942).

## POINT II.

**The Commissioner was given an adequate opportunity to readjust the 1935 return before the statute of limitations had run, which suffices on the issue of notice.**

It is the petitioner's contention that a taxpayer is entitled to a readjustment of the earlier return in the case of a refund or reimbursement in a subsequent year on ac-

count of the unconstitutionality of a tax statute if the earlier year is not outlawed by the statute of limitations.

On the question of notice to the Commissioner, the petitioner agrees with Judge Learned Hand's statement, concerning a refund; namely, that the Commissioner should not on refund of the tax be automatically charged with the duty of scrutinizing the earlier return to see whether a deduction has been made and whether the statutory period has expired for reassessment of the income if a deduction was taken (R. 36). However, the petitioner submits Judge Learned Hand's further statement that to secure a possible reassessment the taxpayer must bring the refund to the Commissioner's notice as soon as he receives it (R. 36), is erroneous, harsh and unsupported by authority.

It is further submitted that the correct approach to the problem of notice to the Commissioner is the following: It should be considered sufficient notice if the taxpayer gives the Commissioner an adequate opportunity to reassess the earlier return before the statute of limitations has prevented such reassessment. If the Commissioner then deliberately or unintentionally permits the statute to run, he should not thereafter be allowed to raise the defense that since a reassessment of the earlier return is barred by the statutory period, the taxpayer must be deemed to have received taxable income in the refund year. The proposed rule is more equitable than the one suggested by Judge Hand.

Moreover, the view adopted by Judge Hand would react most harshly on the taxpayer who frequently is not instantly aware of his right to seek a readjustment of an earlier return, but who subsequently before the statutory period has run, acquires knowledge of this right, and thereafter gives the Commissioner an adequate opportunity to reassess the prior return.

Too, would Judge Hand claim that the Government could not seek to readjust a prior return in the case of a subsequent refund due to the collection of an illegal tax unless the Government served the taxpayer with notice of its intention concomitant with the granting of the refund? The answer is obvious. The Circuit Court of Appeals below would undoubtedly take the position that the Government could reassess the earlier return so long as the statute of limitations had not outlawed such reassessment.

Thus it is apparent that to compel the taxpayer seeking a readjustment of the earlier return to bring the refund to the Commissioner's notice as soon as it is received would be extremely unjust to the taxpayer, and conversely, most biased in favor of the Government.

The petitioner also respectfully submits that the Commissioner did in fact receive an adequate opportunity before the statute of limitations had run to readjust the 1935 return.

The petitioner brought the tax refund to the attention of the Commissioner long before the year 1935 was closed by the statute of limitations; indeed, it offered to include it in income for the year 1935. This offer was never accepted by the Commissioner, who insisted that the proper year in which to reflect the refund was 1936. The taxpayer also offered to pay the amount of tax in 1936, but based on the 1935 rates. The Commissioner refused this offer because the 1936 rates were more than twice as high as the 1935 rates. The Commissioner had the power in this case, based on notices and opportunities repeatedly given to the Commissioner by the taxpayer, to reassess the taxpayer for the year 1935. The affidavit of the taxpayer filed with the Commissioner and sworn to on December 14, 1938, which was long before the statute of limitations had barred the year 1935, shows

that this opportunity had been given to the Commissioner. The Court's attention is directed particularly to paragraphs 7, 8, and 9 thereof (R. 42-43, 40).

## POINT III.

**The Commissioner, before the statutory period has run, should not have the election of reassessing the original tax or including the refund in the later year.**

Petitioner calls special attention to relevant decisions which hold that if the statute of limitations has not run, the Commissioner should reassess the prior return (*Inland Products Co.* v. *Blair, Bergan* v. *Commissioner, Leach* v. *Commissioner, Bohemian Breweries, Inc.* v. *Commissioner, E. B. Elliott Co.* v. *Commissioner, supra*).

Thus Judge Learned Hand's statement that the Commissioner, before the statutory period has expired, may at his pleasure either reassess the original tax or include the refund in the income for the later year (R. 36) is not sustained by any of the cases. To give the Commissioner such an election would be grossly unfair to the taxpayer, for the commissioner would always select the year with the *higher rates.* There would be no tax certainty nor equity in such a rule.

For example, in the *Inland Products Co.* case, *supra,* the Commissioner sought to readjust the prior returns for the years 1919 and 1920, although the refund was made in the year 1924, since there would be a larger deficiency due in income and excess profits taxes than if he had declared the refund taxable income in 1924. The court properly sustained the Commissioner on the basis of correction of a mistake since the statutory period had

not prevented a readjustment of the earlier returns. But in the instant case, where again the statute of limitations was no bar to a readjustment, the Commissioner sought and is seeking to have the refund declared taxable income in 1936, instead of 1935, for the 1936 rates were more than double the 1935 rates. Such inequitable and inconsistent action should not be tolerated by the courts. Here, as in the *Inland Products* case, the Commissioner should have readjusted the prior return since the statutory period did not prevent a reassessment; otherwise, the Commissioner would be permitted to follow inconsistent courses and allowed to completely disregard principles of accounting and law at his whim.

It is respectfully submitted that, as Judge Parker pointed out in the *Inland Products Co.* case, *supra*, the present situation deals with the correction of a mistake between the Government and the taxpayer, and the principles to be applied are those applicable to the correction of such mistakes. There is really but one important issue herein involved; namely, whether the taxpayer, after receiving reimbursements of the invalidated A. A. A. taxes may, before the statutory period has expired, readjust the 1935 income tax return to eliminate the expense deduction The issue should on principle and authority be answered affirmatively—that the tax year 1935 should be revised.

## Conclusion.

Petitioner respectfully submits the petition for writ of certiorari should be granted, for the Commissioner should have readjusted the original deduction in the 1935 tax return since the statutory period had not expired; and furthermore, the petitioner did in fact give the Commissioner an adequate and sufficient opportunity to re-

adjust the 1935 return before the statute of limitations had run. In addition, the Commissioner, before the statute of limitations has run, should not at his pleasure be permitted either to reassess the original tax or include the refund in the income for the later year.

Respectfully submitted,

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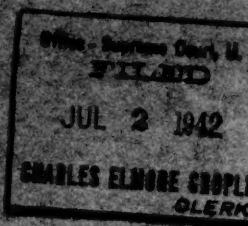


No. 120

# In the Supreme Court of the United States

OCTOBER TERM, 1942

BEN BIBBERG & CO., INC., PETITIONER

*v.*

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT*

BRIEF FOR THE RESPONDENT IN OPPOSITION

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# In the Supreme Court of the United States

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## BRIEF FOR THE RESPONDENT IN OPPOSITION

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### OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 21–25) is not officially reported. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 33–36) is reported at 126 F. (2d) 412.

### JURISDICTION

The decision of the Board of Tax Appeals was ordered affirmed on March 7, 1942 (R. 33–36), but no judgment was then entered. A petition for rehearing was denied on March 27, 1942 (R. 45), and

the judgment of the Circuit Court of Appeals was entered on that day (R. 46). A second petition for rehearing was denied on May 23, 1942 (R. 57). The petition for a writ of certiorari was filed June 5, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

### QUESTION PRESENTED

The petitioner, a dealer in cotton goods, received reimbursements in 1936 from its vendors on account of processing taxes which had been included in the price of goods purchased by it in 1935. The amount of those taxes had already been reflected to petitioner's advantage in its income tax returns for 1935, and the question presented is whether the Commissioner erred in treating the reimbursements as income for 1936.

### STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the statute and regulations involved are set forth in the Appendix, *infra,* pp. 9–11.

### STATEMENT

Petitioner brought this suit in the Board of Tax Appeals to obtain a redetermination of a deficiency in income tax for 1936 which with penalty amounted to $3,381.77. It also sought a refund in taxes for that year in the amount of $954.60 (R. 2–17). The Board found the following facts:

Petitioner is a wholesaler and jobber of cotton goods. Its general practice is to obtain orders

from its customers for specific merchandise and then place the orders with well-known mills. When these mills are ready to ship the goods, they ship them directly to the customers for the account of petitioner. The mill or other supplier sends an invoice to petitioner, and petitioner simultaneously invoices its customer with the goods in question. In some instances petitioner fills orders from a small inventory kept on hand (R. 22).

In the latter part of 1935, members of the cotton industry believed that the Agricultural Adjustment Act would be invalidated by the Supreme Court. Petitioner and other firms accordingly included in their purchase contracts clauses to the effect that if the Act were invalidated, the amount of processing taxes included in the purchase price of the cotton involved would be refunded or credited to them by their vendors (R. 22).

After this Court held the Agricultural Adjustment Act unconstitutional on January 6, 1936, the vendors who had agreed to include the above-mentioned clause in petitioner's purchase contracts promptly issued purchase allowances or credits to petitioner or, in some instances, made cash refunds. In all, during 1936 petitioner received from its vendors credits or other reimbursements in the sum of $19,763.13. This represented the amount of processing taxes charged to petitioner on goods which it purchased in 1935. With certain small exceptions, petitioner sold all these goods before December 31, 1935 (R. 22–23).

Petitioner kept its books on the accrual (and calendar year) basis. In its return for 1935 it included the $19,763.13 in processing taxes as part of the cost of the goods sold by it. In its return for 1936, which it did not file until January 28, 1938, it reported $7,729.45 of the $19,763.13 as income. The balance of $12,033.68, which it did not report in its return, represented sums covered by credit memoranda dated in 1936 which it had executed to some of its vendees for processing taxes included in the purchase price charged them. But on March 15, 1937, it had cancelled all of the credit memoranda. No reimbursement of the $12,033.68 was ever made by petitioner to its vendees, nor did petitioner have any contracts with its vendees to reimburse them for any processing taxes which petitioner might have passed on to them. Its books for the year 1935 contained no accounts indicating any amount due from its vendors for refund of processing taxes or reflecting any liability to its vendees for the taxes (R. 23–24).

By letter dated January 3, 1940, petitioner was notified of deficiencies in its tax for 1936. The Commissioner determined that petitioner realized income in 1936 on the full amount of the reimbursements received by it in that year and that it was liable for the prescribed penalty for failure to have filed its 1936 return on time (R. 10–13, 22). The Board sustained his determination and found that the deficiencies properly were assessed (R. 22–26). The Circuit Court of Appeals affirmed (R. 36, 46).

Thereafter, the court denied two petitions for rehearing in which petitioner alleged that prior to the date of expiration of the statutory period within which its 1935 tax might have been adjusted, it had notified the Commissioner of the reimbursements and had offered to have them added to its taxable income for 1935, when lower rates were in effect (R. 37–57).

ARGUMENT

1. Petitioner does not dispute (Pet. 5, 7) that the Commissioner may treat reimbursements such as those here involved as income in the year received in cases where the expiration of the statutory period of limitation precludes adjustment of the tax for the earlier year. See *Houbigant, Inc.* v. *Commissioner,* 31 B. T. A. 954, affirmed 80 F. (2d) 1012, certiorari denied, 298 U. S. 669; *Nash* v. *Commissioner,* 88 F. (2d) 477 (C. C. A. 7), certiorari denied, 301 U. S. 700. But it contends (Pet. 5, 6–9) that if the Commissioner is afforded adequate opportunity to make the adjustment within the period, he should be required to do so and should not have the alternative of treating the reimbursements as income in the year received. It asserts (Pet. 5) that in the instant case it gave the Commissioner several such opportunities to reassess its 1935 tax.

This assertion is unsupported by any evidence in the record (see R. 39). As appears from the record references cited by petitioner (R. 40, 42–43), it is based only on allegations contained in the petitions

for rehearing and on an affidavit filed by petitioner in support thereof in the court below.[1] The court below declined to decide whether the Commissioner would have been required to make an adjustment for 1935 if petitioner had notified him of the reimbursements as soon as it received them, pointing out that petitioner did not give any such prompt notice but, on the contrary, reported a portion of the reimbursements as income in its return for 1936 (R. 36). In view of these circumstances and of the fact that the burden of proof was on petitioner, the case does not present the question urged in the petition.

2. The decision of the court below does not conflict with *Inland Products Co.* v. *Blair, Commissioner,* 31 F. (2d) 867 (C. C. A. 4), or *Leach* v. *Commissioner,* 50 F. (2d) 371 (C. C. A. 1). The issue in each of those cases was whether the Commissioner had erred in adjusting the tax for the

[1] The affidavit (R. 42–44, 54–56) is to the effect that on December 14, 1938, petitioner protested in writing the Commissioner's proposed assessment of a deficiency tax for 1936 on the ground that the $12,033.68 in reimbursements not reported by it in its return for 1936 should be charged as income for 1935. The statutory period of limitation for adjusting the 1935 tax presumably expired subsequent to December 14, 1938, but precisely when is uncertain since the record does not contain petitioner's return for 1935 or disclose the date when it was filed. Under Section 275 (a) and (c) of the Revenue Act of 1934 (48 Stat. 680) the statutory period expired three years after the date of filing the return unless an amount of gross income equal to more than 25% of the total reported was omitted, in which case the period was five years.

earlier year, and neither court passed on the question whether he had the alternative of treating the refunds involved as income for the year of receipt. In the instant case the court below agreed (R. 34–36) that the Commissioner properly might have adjusted the tax for 1935. It held only that in the circumstances he was not required to do so.

3. Petitioner suggests (Pet. 8–11) that under correct accrual principles the reimbursements constituted income for 1935. During that year, however, petitioner had only a contractual right which was expressly contingent upon whether the Agricultural Adjustment Act would be declared unconstitutional (R. 19, 22, 24–25). The contingency did not occur until 1936. Accordingly, not until then did petitioner's right to the reimbursements become fixed and accruable. *United States* v. *Anderson*, 269 U. S. 422, 441; *Lucas* v. *American Code Co.*, 280 U. S. 445; *North American Oil* v. *Burnet*, 286 U. S. 417; *United States* v. *Safety Car Heating Co.*, 297 U. S. 88. There are no decisions to the effect that petitioner properly might have accrued the amount of the reimbursements on its books for 1935 and it did not attempt to do so (*supra*, p. 4.)[2]

[2] *Sanford Cotton Mills, Inc.* v. *Commissioner*, 42 B. T. A. 190, and other similar decisions of the Board of Tax Appeals relied on by petitioner (Pet. 8–9) do not conflict with the instant decision. Those cases involved taxpayers in the situation of petitioner's vendors whose liabilities in the year in which they were allowed deductions were fixed and unconditional in that the amounts involved necessarily were required to be paid out by them either as taxes to the Government or to their vendees pursuant to contract.

The Government has petitioned for certiorari in *Helvering* v. *Estate of David Davies,* No. 118, 1942 Term, but the granting of the petition in that case does not require similar action here. There, the taxpayer sought to deduct in 1935 processing taxes which he never paid and which he was then contesting; and the Government is there contending that the accrual system of accounting does not permit the accrual of items of deduction which the taxpayer is contesting. Here, on the other hand, the petitioner actually paid the amounts in question in 1935, they were properly reflected in its returns for that year, and the question is merely whether the actual reimbursements in 1936 constitute income for 1936.

### CONCLUSION

There is no conflict of decisions. The petition should be denied.

Respectfully submitted.

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JULY, 1942.

## APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from * * * the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

SEC. 41. GENERAL RULE.

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *

SEC. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED.

The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under section 41, any such amounts are to be properly accounted for as of a different period. * * *

* * * * *

SEC. 291. FAILURE TO FILE RETURN.

In case of any failure to make and file return required by this title, within the time

prescribed by law or prescribed by the Commissioner in pursuance of law, unless it is shown that such failure is due to reasonable cause and not due to willful neglect, there shall be added to the tax: 5 per centum if the failure is for not more than thirty days with an additional 5 per centum for each additional thirty days or fraction thereof during which such failure continues, not exceeding 25 per centum in the aggregate. * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 42–1. *When included in gross income.* * * * gains, profits, and income are to be included in the gross income for the taxable year in which they are received by the taxpayer, unless they are included as of a different period in accordance with the approved method of accounting followed by him. * * * If no determination of compensation is had until the completion of the services, the amount received is ordinarily income for the taxable year of its determination, if the return is rendered on the accrual basis; or, for the taxable year in which received, if the return is rendered on the receipts and disbursements basis. If a person sues in one year on a pecuniary claim or for property, and money or property is recovered on a judgment therefor in a later year, income is realized in the later year, assuming that the money or property would have been income in the earlier year if then received. This is true of a recovery for patent infringement. Bad debts or accounts charged off subsequent to March 1, 1913, because of the fact that they were determined to be worthless, which are sub-

sequently recovered, whether or not by suit, constitute income for the year in which recovered, regardless of the date when the amounts were charged off. (See article 23 (k)–1.) Such items as claims for compensation under canceled Government contracts constitute income for the year in which they are allowed or their value is otherwise definitely determined, if the return is rendered on the accrual basis; or, for the year in which received, if the return is rendered on the basis of cash receipts and disbursements.

U. S. GOVERNMENT PRINTING OFFICE: 1942

IN THE

# Supreme Court of the United States

**October Term, 1941.**

No. 120.

BEN BIMBERG & CO., INC.,
*Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,
*Respondent.*

***Reply Brief in Support of Petition for Writ of Certiorari.***

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## Reply Brief in Support of Petition for Writ of Certiorari.

Petitioner would like to emphasize that the primary question before this Court is whether the reimbursements received by petitioner from its vendors should be declared taxable income in 1935 or in some other year.

This question was presented to the United States Board of Tax Appeals, which rendered its decision *on the merits* sustaining the Commissioner's treatment of these reimbursements as income for 1936. In upholding the Commissioner the Board simply rejected petitioner's contention that the reimbursements should be declared taxable income in 1935 and that the 1935 return be readjusted (the statutory period not having expired).

The Commissioner, before the Board of Tax Appeals, never even argued that petitioner gave him no notice or adequate opportunity to readjust the 1935 return. He merely insisted that the reimbursements were taxable in-

come in 1936. This position was assumed because the Commissioner knew as a result of petitioner's filing with him of an affidavit dated December 14, 1938 (R., 42-44), and as a result of earlier protests and proposals that petitioner desired a readjustment of its 1935 tax return. The only point of controversy in the 1936 return was the petitioner's repeated assertion that the A. A. A. reimbursements were not taxable in 1936; in all other respects except that, the tax return was mutually acceptable to petitioner and Commissioner.

The three year statutory period in the instant case expired March 15, 1939 since the 1935 return was filed about March 15, 1936 (Section 275 [a] [c] of Revenue Act of 1934—Appendix "A"). On December 15, 1938, the Commissioner received formal notice in writing (protest in affidavit form) of petitioner's position. This was after prior informal notices and opportunities had been given the Commissioner to readjust the 1935 return.

In view of the foregoing, before the Court of Appeals for the Second Circuit the Commissioner was naturally silent on the question of notice, and stated in his brief that the *sole question* presented was:

> "Where the petitioner was properly allowed certain deductions in 1935, was the Commissioner warranted in including as income for 1936, reimbursements received or accrued in that subsequent year?" (p. 2).

The Commissioner, knowing that he had received an adequate opportunity to readjust the 1935 return, argued in his brief that regardless of whether or not the earlier year was closed by the running of the statute of limitations, the reimbursements should be declared taxable income in 1936 (pp. 15, 16-17). He concluded on page 17 of his brief:

> "It thus becomes clear that the only workable rule requires that the refund should be taxed in the later year, regardless of whether the earlier year is still open."

It is apparent that before the Second Circuit Court of Appeals the Commissioner did not assert that the petitioner failed to give him an adequate opportunity to readjust the 1935 return. Instead, he chose to follow the aforesaid approach.

Thus, petitioner was shocked when Circuit Court Judge Learned Hand in deciding the instant case went off on a tangent, and based his decision on a ground not even raised by the Commissioner. Furthermore, there was nothing in the record to justify the *Court's assumption* that no opportunity was given the Commissioner to reassess the 1935 return. In fact, the Commissioner, since he had received ample notice, argued the sole point in his brief that the refund should be taxed in the later year regardless of whether the earlier year was still open (pp. 15, 16-17).

And even now before the United States Supreme Court the Commissioner (in his brief in opposition to this petition for certiorari) states that the question presented " * * * is whether the Commissioner erred in treating the reimbursements as income for 1936" (p. 2)—again maintaining a discreet silence on the question of notice.

Petitioner, being aggrieved, respectfully requests this Court to grant the petition for certiorari for the reasons stated therein and in its brief in support thereof.

Too, the Government has petitioned for certiorari in *Helvering* v. *Estate of David Davies,* No. 118, 1942 Supreme Court Term, reported at 126 F. (2d) 294, 1942 P-H par. 62, 533 (C. C. A. 6, March 5, 1942), and it is also respectfully urged that the granting of the petition in that case requires similar action here.

In the *Davies* case, the Government is seeking to readjust the 1935 return of the taxpayer therein to eliminate the deduction claimed. In the case at bar, the petitioner insists that the same procedure be followed.

In the *Davies* case, $59,049.44 of the total sum deducted was deposited in escrow in 1935 pursuant to a restraining order against the Collector of the taxes. The sum of $65,861.25 was accrued on the books of the taxpayer as a debit to "merchandise purchases, hog tax or pork" and as a credit to accounts payable. In the instant case, the petitioner's books, also kept on the accrual basis, did show the full amount of taxes in question, $19,763.13 as a deduction from gross income. In determining its taxable income for the year 1935, petitioner considered the sum of $19,763.13 as part of the cost of goods sold (R., 24, Pet. 3).

In both cases, according to the weight of authority, (Pet. 7) the Government should readjust the 1935 return (the statutory period not having expired) to eliminate the deduction claimed and thereby truly reflect the taxpayer's 1935 income.

Counsel would also like to point out that the Court of Appeals for the Eighth Circuit in *Cannon Valley Milling Co.* v. *Commissioner,* (Alex. Federal Tax Service, par. 20,872) has affirmed the decision of the United States Board of Tax Appeals, 44 B. T. A. 763 (1941) relied upon by petitioner at page nine of both his petition and brief in support thereof.

The Eighth Circuit Court of Appeals holds that processing taxes collected by a corporation in 1935 and returned to its customers in 1937, after the A. A. A. was declared unconstitutional in 1936, is deductible in 1935, the year in which the sales occurred, and not in 1937 (the year of refund) as alleged by the Government.

It should logically follow, in addition to it being proper accounting practice, that if the vendor is entitled to a

deduction in 1935, petitioner, as vendee, must be deemed to have received taxable income in that very same year (see petition, p. 9, and main brief, p. 10).

In this connection counsel calls the Court's attention to *Greer-Robbins Co.* v. *Commissioner,* 119 F. (2d) 92, 1941 P-H par. 62,605 (C. C. A. 9, 1941) and the connected case of *Commissioner* v. *Union Motors, Inc.,* 119 F. (2d) 93, 1941 P-H par. 62,606 (C. C. A. 9, 1941), where the Court of Appeals for the Ninth Circuit held that where accrued interest owed an affiliate company is deductible in 1935 the affiliate company must be deemed to have received taxable income in the same year.

It is respectfully submitted that the same principle should be applied to the case at bar and the petitioner should be held to have received taxable income in 1935 with respect to the A. A. A. reimbursements received.

## CONCLUSION.

### The Petition Should Be Granted.

Respectfully submitted,

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## APPENDIX "A".

Revenue Act of 1934 (48 Stat. 680)

Sec. 275 (a):

The amount of income taxes imposed by this title shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

Sec. 275 (c):

If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.